SG Capital Research

Global Market Insights

Research Note – Interim Update (A# 2)

MAEG- INTERIM UPDATE # 02 SG 2010 # OCT 14

For Immediate Release – Thursday AM (EST)

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Market Strategy Global (A # 2) - SPX – Closed @ 1178

We have picked up charts (below) that has some distinct characteristics from observation & Special Situation this week based on our assessment:

- ## Special Coverage

- **QE 2**
- **USD**
- **SPX EARNIGS / INTC /SMH**
- **SENTIMENTS US / EUROPEAN**
- **SPX ST / MT**
- **SPX – TRIN / SPX ARMS**
- **NASD**
- **XLF / XHB**
- **TLT**

• SPX Signals & Price Projections (update signal)

- *2010 YTD – This year, we have had (3) clean TREND SIGNALS from " POM 12 to POM 14 " rise (each of 7.5%, 7.0% % 10.0 %) for Longs Ideas & (1) POM 15 to POM 13 (drop of 9%) for Net Short Ideas and Risk managed Jan POM 14 decline (drop of 9 %)*

- *Currently we are on POM 14 – Re run (for Fully Hedged positions) and SPX is extended by 6.7% but we are not able to capitalize on it for NET SHORT, till it triggers POM 15 within POM – RA / RI framework . We are seeing some signs of POM 15 Re run here. The base criteria for it is to have min (3) of the broader Indices to double tops and rejects. We see DOW, NASD & NYA almost in that vicinity and once complete then we will assess the other internal criteria to confirm. (On different POM 15 Note - Silver had 2nd Gap yesterday of 3 Gap play , We have some POM 15 criteria for Gold POM 15)*

- *Extension of 6.7% is more than we would like to have. The worst extension in past 4 yrs have been 7.5% of 40 days but that was converted to POM 15 (NET SHORT) and currently we are on day 30th of extension of POM 14 re run. The Last POM 15 in April resulted in a CRASH !!*

- *Patience is what it may be at as we are looking to evaluate a drop to POM 13 or POM 12 after this rally to asses " The seasonality or Presidential Cycle" if we need to turn Bullish. Or Even to see the impact of QE 2. On Pull back we are looking for DEATH CROSS of past 1115 to be the GOLDER CROSS of future or check for something more serious. (Time will tell, let us wait and watch)*

• Trading & Investment Conclusions

- ***Accumulations continues in the "SETUP - PQV VALIDATED EQUAL WEIGHTED PORTFOLIO (in Section E – MAEG) during this SPX extension of 6.7 % with desired price points & scaled entry @ the Mean Confluence Zone on the weakest Equities in Setup # 2 capitalizes it (within RA / RI, these Equities to be Monitored with Risk management factors).***

- ***The current 3rd Re run - POM 14- @ 1104 is to "Hedge Long position" on ideas that were triggered at POM 12 @ SPX 1020 in July 2010 for rally and / Or the last POM 13 at 1045 for a bounce (with above ideas).***

- ***"Net Short Position" should come in at POM 15 Re and we have no indication of that signal. Therefore we stay with***

our original Intermediate POM 15 @ 1200 OF April is still Intact.

- ## Market Insights

Market continues to be driven by USD. This has not only caused extension in Foreign currency markets but has all the Red Flags of market internal issues completely ignored but if history is any guide it all comes back to earth and this too shall pass. It's likely to be a classic case of 'buy the rumor and sell the fact." To much news is getting priced in and market goes up on Good news. I worry !. I don't want to sound Bull or Bear but want POM 12 or 15 for next actionable Idea regard less of surrounding noise..

One thing for sure is how the Venus Retrograde played upon human sentiments past few days , If it was a bottom instead of Top market would be Selling of 300 points a day (I have chart released then to demonstrate that in March 09 when only 4 planets lined up instead of current 6 planets). Sometimes it amazes when all issues come together at once. The Anniversary of 11th Oct 2007 Top coincides with other elements. Not to mention SPX 1180 is the breakdown area of Flash Crash that is suppose to increase the volatility due to order imbalances of past. Just like SPX 1200 during the test of April 2009 – Lehman Crash date of Sept 2008

We certainly have high level of investor complacency. Lot of famous investors and managers embarrassed not making public comments about their bearishness any more. That leaves most of those being vocal being bulls, which also helps the momentum

Here is QE 2 Support from FOMC .members. This is not a fair balance, anyone can change mind quick, its important to know how long the group be to gather with this view. Especially as we go into Congress hearings ,

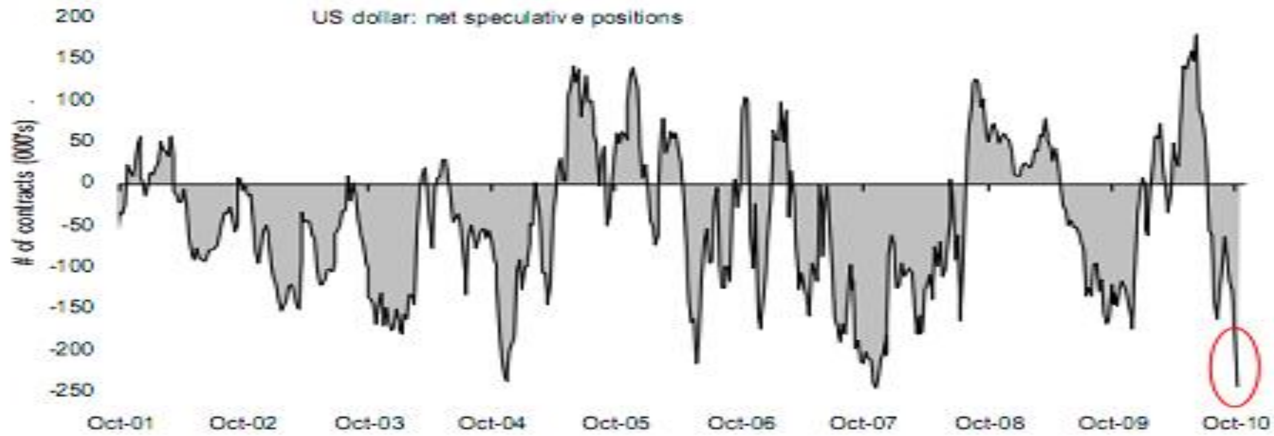
Where FOMC Members Stand on QE II			
Hawks (don't support QE and willing to dissent)	**Soft Hawks** (don't necessarily support QE but will go along with Chairman)	**Neutral** (will vote with the Chairman)	**Doves** (in favor of QE)
Fisher Hoenig* Lacker Plosser	Kocherlakota Lockhart Warsh*	Duke* Pianalto* Bloom Raskin* Tarullo*	Bernanke* Bullard* Dudley* Evans Rosengren* Yellen*
* 2010 Voting FOMC Member			

USD

Since the dollar has been ruling all the capital markets . Based on the net speculative positions in the USD there is a very high **chance** (based on past occurrences) that the dollar will rally from here. See the table published by Reuters, the US dollar has rallied 100% of the time from these levels on a 3 month basis. On a 1, 2 and 6 month basis it has rallied 80% of the time:

QE has been fully priced into the dollar and this decline in the dollar has contributed substantially to the rally in risk assets in recent weeks. The dollar is extremely oversold and out of favor. Even a short-term rally in the dollar would likely be a quick negative for the stock market. Currently its been banging the lows with far lesser contracts then past few days.

Extreme Sentiment Readings - The currency markets are also flashing extreme sentiment readings. Just six months ago the euro was said to be totally doomed. The percentage of euro bulls fell to low single-digit readings. Now, after a nice rally from below 1.20 to around 1.40 the number of euro bears has declined to low single-digits. It looks like we have come full circle here, and the euro rally is about to end. Yet bullish sentiment has reached record levels! Sentiment extremes are typical signs of very lopsided trades. And usually a trend reversal is right around the corner. Sentiments exactly opposite on Dollar.



Extremely bearish $ speculative positions	Performance of TWI$ after				
	1m	2m	3m	6m	12m
Jan-04	1.3%	3.6%	4.2%	3.2%	-2.9%
Nov-04	-0.1%	-0.5%	0.6%	3.2%	8.6%
May-06	2.8%	3.2%	2.0%	0.9%	0.0%
Nov-07	0.6%	1.3%	0.4%	-2.5%	8.3%
Dec-09	3.7%	4.2%	5.2%	10.1%	0.9%
Average	1.7%	2.4%	2.5%	3.0%	3.0%
Median	1.3%	3.2%	2.0%	3.2%	0.9%
% times outperform	80%	80%	100%	80%	60%

Source: Thomson Reuters,

EARNINGS

INTC – point 1

Yesterdays rally really got Jump start from INTC and then by JPM . The positive reaction remained in the rest of the market until mid-afternoon, but then the overall market rolled over, and although closing positive, did so with a negative pattern of strength in the morning and weakness in the afternoon. Both stocks open much higher and closed lower specifically INTC. Here is INTC ‘s reaction after past 4 Qtrs. The money flow is horrendous.

INTC Gaped up 2% and closed down 4% when Market was up 100 points

SMH – Point 2

SMH closed down 1% when Market was up 100 points


Daily Semiconductor Sector
Bottoms-up Money Flow
Money flow divergnces
'091008
'091126
'100114
'100304
'100422
'100610
'100729
'100916
'101104
'101223
'110210

SPX – Point 3

After INTC 's earnings SPX takes over along with INTC. Here are the results of past 4 Qtrs (Note last year 2009, it happened as well and Seasonality rally started after earnings corrections of 6% . (We have repeated this chart from Monday to link it together)

<u>Earnings Picture -</u>

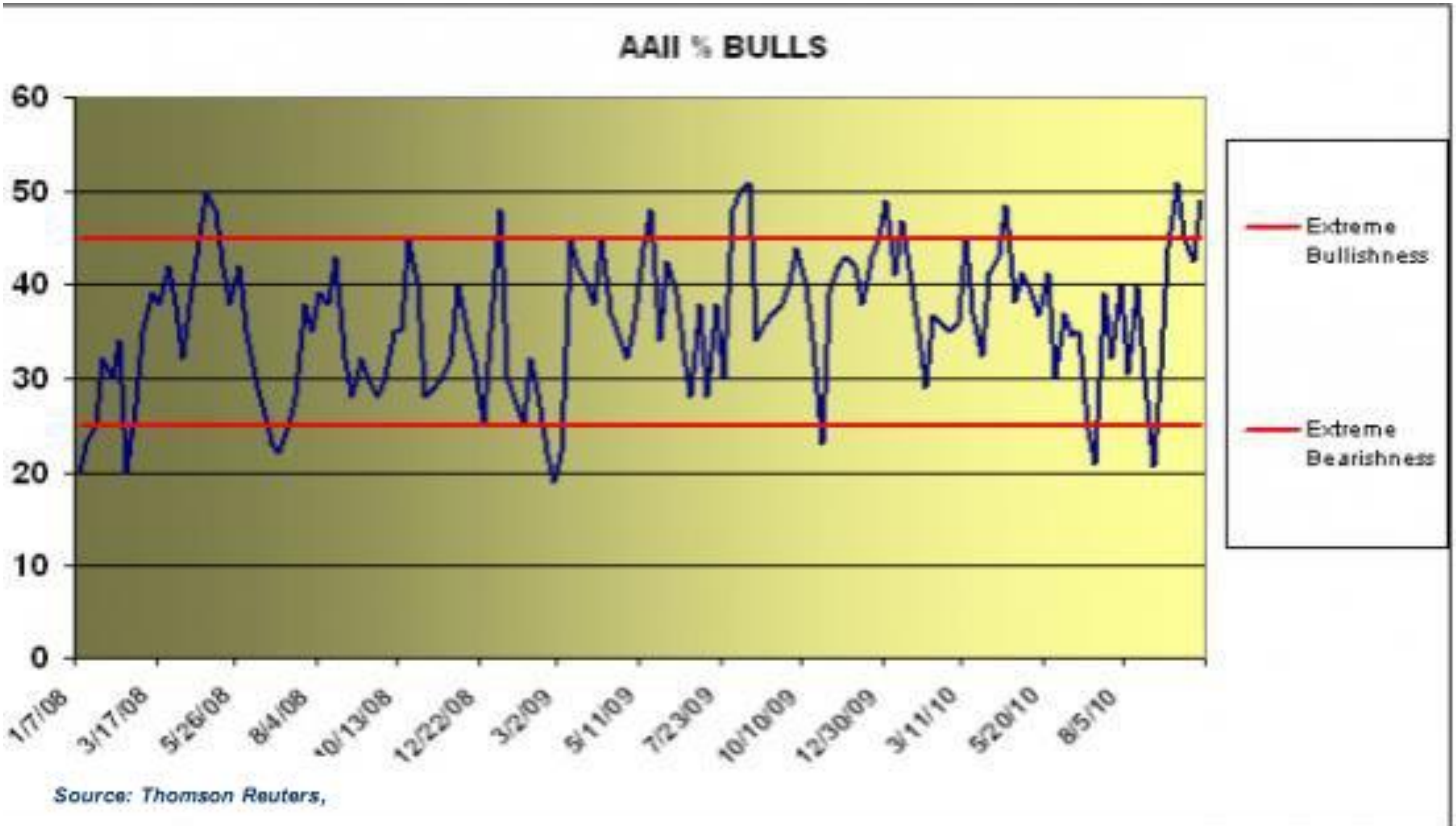
David Rosenberg's Propriety fair-value model moved down to 1,050 in the past month from 1,070, with regard to the S&P 500. The range is 1,000 to 1,120. The Index is at the top end of the band, suggests an overvaluation of 10% -- the last time it was this overvalued was late last year;

The Shiller normalized P/E ratio is now pointing towards a near-30% degree of overvaluation;

Tobin-Q model that looks at replacement-historical costs indicates a 20% level of overvaluation.

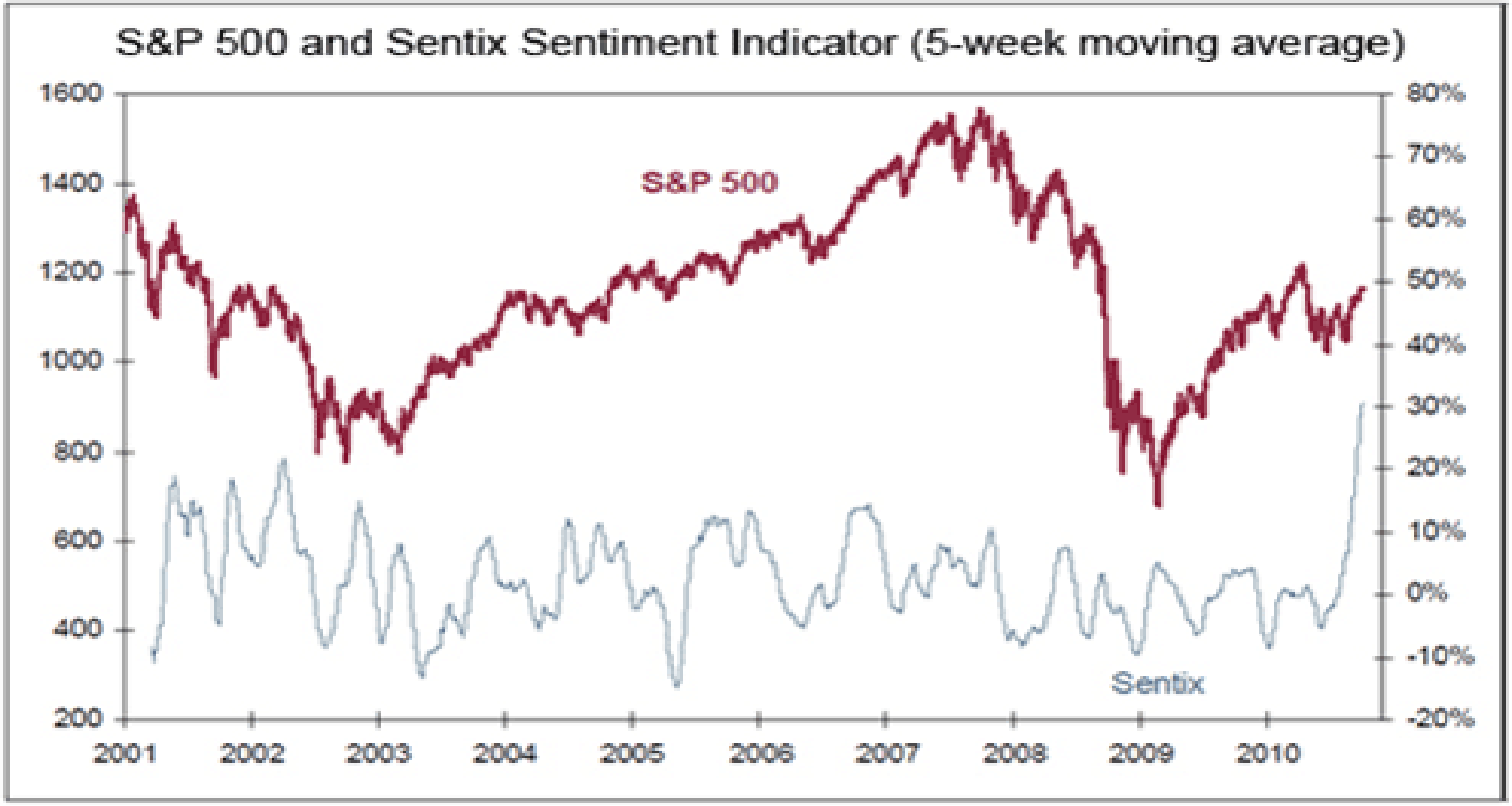
<u>SENTIMENTS</u>

(AAII) reached the warning level above 50% bullish , and there had only been three other times since 2007 when it reached that level, one being just before the peak topped out on October 11, 2007, and once in May of 2008 just before the big bear market rally ended in May 2008. And it reached 48.5% bullish just a week or so before the April top this year.



European Sentiments

As you can see on the chart below the Sentix took a huge jump, reached the highest reading since it was invented in 2001. The most amazing aspect of this reading is the fact that markets have gone nowhere for nearly 12 months!



Source: BHF-Bank

SPX – Hourly

Green price path is chased by traders who love this pattern, See the chart below , Since it's a diagonal triangle, a sharp decline will follow the next top. That's just the way diagonal triangles play out at the end The sharply rising support line shows anxiousness

SPX –

Breadth is rapidly diminishing and a correction here could be a setting up. However, according to the wave count, time and price are running out:

SPX – Important chart # 1 – This is a forward looking Indicator and Internals of Market

The SPY/Trin ratio normally peaks out two to four weeks before the SPY sees it peak, Its been three weeks thus far. Also the SPY/Trin ratio hit a high reading and suggest something bigger then a consolidation. There are cycles for a low that come in end October or early November and are when we are expecting the next intermediate term low to form.

<u>SPX – Important chart # 2 - This is a forward looking Indicator and Internals of Market</u>

1999 to 2010 . The bottom window is the SPY/TRIN ratio. Previous highs since the April occurred when the SPY/Trin ratio reached above 140. Notice that the current SPY/Trin ratio is higher now then the previous two high that occurred at the April and June high. If you look back **and compare the current SPY/TRIN ratio with the 2007 and 2000 major top ratios**, the current reading is not far from those levels. According to the current SPY/TRIN ratio a top is not far off.

NASD

NASD has rallied and clearly broken out above the trendline that marked the top of a usually negative 'megaphone formation'. With the negative divergence by its internal strength, as measured by its Relative Strength making lower highs), and how that usually results in the divergence being resolved by RSI being correct with the direction, and the market rolling over to the downside. MACD has flattened out And we could note that if a correction begins, a decline to either of the trendlines at the bottom of the megaphone formation would a substantial decline. Lest wait and see. Now its also Forming a Double Top. We have our Player for POM 15

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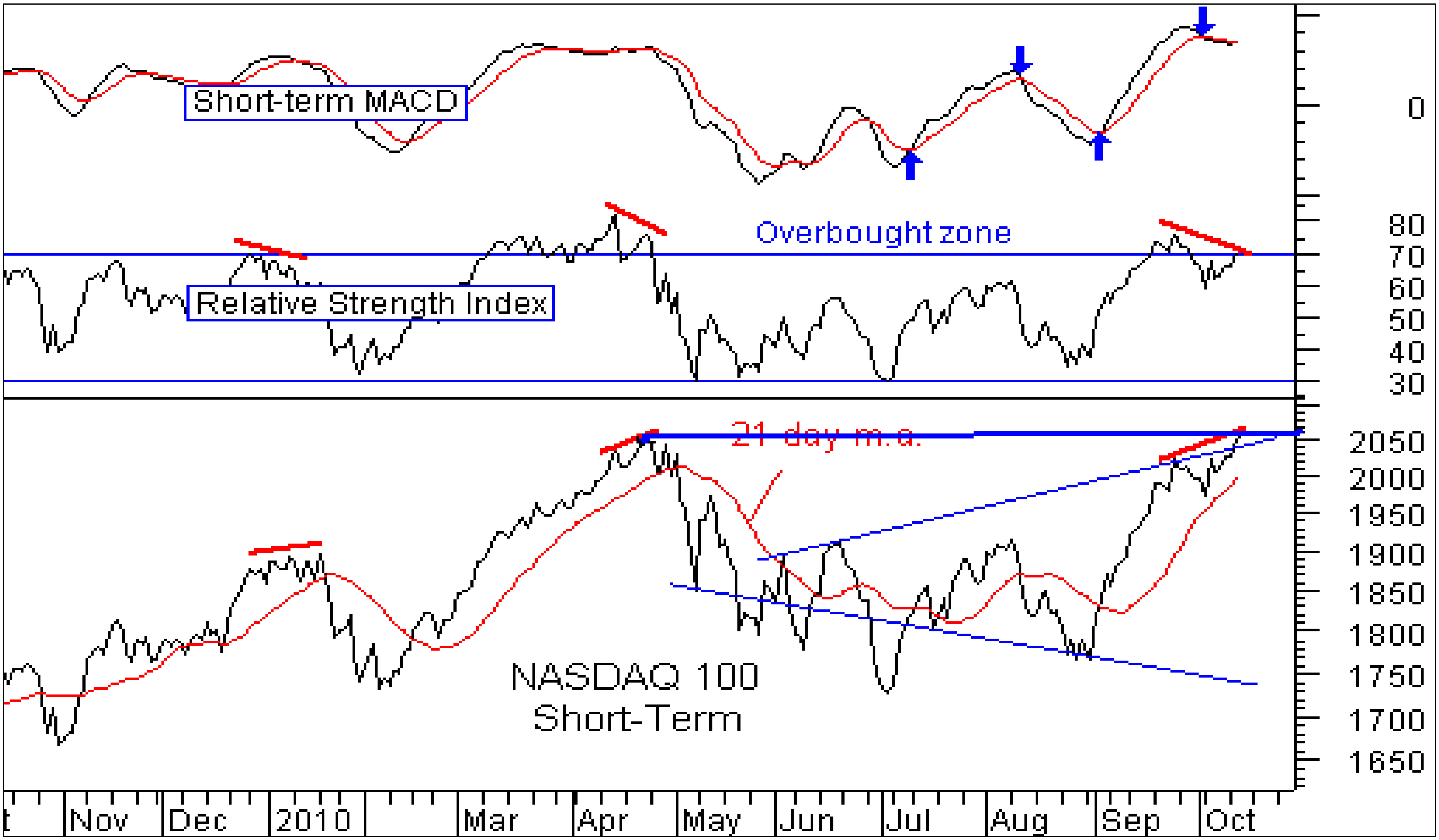

XLF

XLF finance sector remains the big laggard, X**LF opened strong and closed weak yesterday in spite of 100 points move on DOW** . The indicator window shows the price relative (XLF:SPY ratio). Even with the move to resistance, XLF remains an underperformer. All QE 2 money should be going into this stocks which has been source of the problem.

XHB

Home builders , same story as XLF - All QE 2 money should be going into this stocks which has been source of the problem.

- **TLT - Weekly– 3 Year with RSI, CCI, MACD**

(11 W / 40 W SMA)

TLT - Daily – 3 Year with RSI, CCI, MACD

(11D / 55D)

Day Session
Last 103.05
High on 08/25/10 109.34
Average 95.8626
Low on 04/07/10 87.30
SMAVG on Close(55) 103.5855
SMAVG on Close(11) 104.5264
Volume 0.00
RSI on Close(14) 44.69
CMCI (13) -212.57
MACD on Close(12,26) 0.0059
Signal on Close(9) 0.2217
110
100
95
90
15m
5m
0.00
100
50
0
200
0
-200
2.00000
1.00000
0.00000
-1.00000
Sep
Oct
Nov
Dec
Jan
Feb
Mar
Apr
May
Jun
Jul
Aug
Sep
2009
2010
TLT US: iShares Barclays 20+ Year Treasury Bond Fund G2 Daily 8/18/09 to 10/14/10
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2 – TLT- PEC Analysis

Treasury Bonds If we look at TLT we can see that we are now at a place where PEC D has occurred at 105 , it nailed it again but there was no conformation from POM

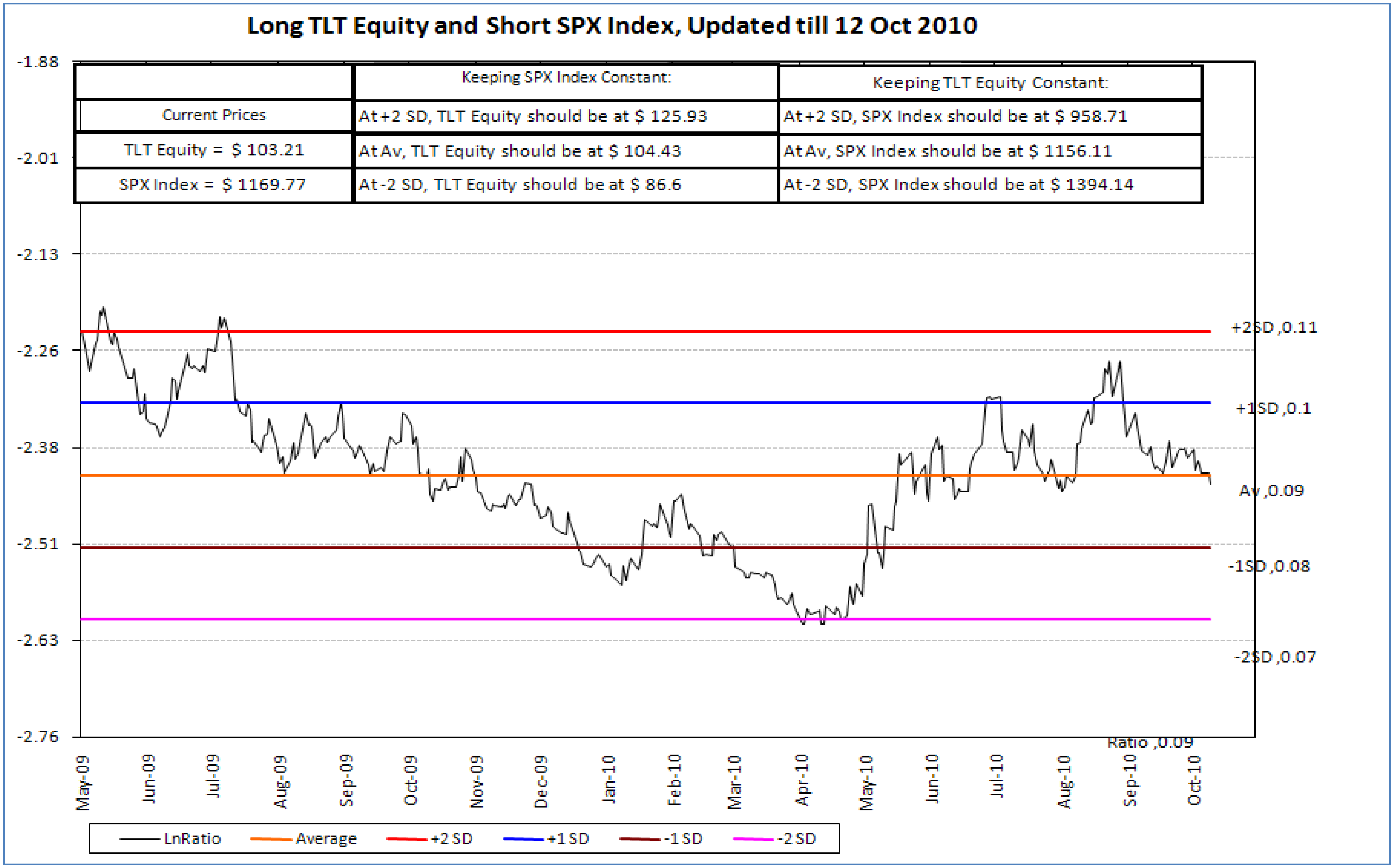
2 – TLT- POM - Price , Volume & Pattern Analysis

By this method both High volume highs and High volume lows (marked In green) both needs to be tested to prove the point to reject or diverge , Past few week its been moving towards high volume lows and towards the trend lines. Once the test is complete we will have clear picture. <u>So its inconclusive POM / PQV</u> . SD chart below on Correlation also is at Neutral zone <u>that is inconclusive as well</u> (Once we get all lined up it will confirm the trade , Keep a watch)

2 – TLT- POM - Price , Volume & Pattern Analysis

We could not get update on above chart so used different data source to represent this

TLT – Correlation Ratio Analysis with SPX – 365 days Time basis



	Keeping SPX Index Constant:	Keeping TLT Equity Constant:
Current Prices	At +2 SD, TLT Equity should be at $ 125.93	At +2 SD, SPX Index should be at $ 958.71
TLT Equity = $ 103.21	At Av, TLT Equity should be at $ 104.43	At Av, SPX Index should be at $ 1156.11
SPX Index = $ 1169.77	At -2 SD, TLT Equity should be at $ 86.6	At -2 SD, SPX Index should be at $ 1394.14